

# EXAMINING UNETHICAL PRACTICES IN THE STUDENT LOAN INDUSTRY

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## HEARING

BEFORE THE  
COMMITTEE ON  
EDUCATION AND LABOR  
U.S. HOUSE OF REPRESENTATIVES  
ONE HUNDRED TENTH CONGRESS  
FIRST SESSION

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HEARING HELD IN WASHINGTON, DC, APRIL 25, 2007

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## **EXAMINING UNETHICAL PRACTICES IN THE STUDENT LOAN INDUSTRY**

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**Wednesday, April 25, 2007  
U.S. House of Representatives  
Committee on Education and Labor  
Washington, DC**

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The committee met, pursuant to call, at 10:33 a.m., in Room 2175, Rayburn House Office Building, Hon. George Miller [chairman of the committee] presiding.

Present: Representatives Miller, Kildee, Payne, Andrews, Hinojosa, McCarthy, Tierney, Kucinich, Wu, Davis of California, Bishop of New York, Sestak, Loeb sack, Hirono, Altmire, Yarmuth, Hare, Courtney, Shea-Porter, McKeon, Petri, Hoekstra, Castle, Ehlers, Platts, Keller, Kline, Kuhl, and Walberg.

Staff present: Aaron Albright, Press Secretary; Tylease Alli, Hearing Clerk; Jeff Appel, GAO Detailee; Adrienne Dunbar, Legislative Fellow, Education; Sarah Dyson, Administrative Assistant, Oversight; Gabriella Gomez, Senior Education Policy Advisor (Higher Education); Ryan Holden, Senior Investigator, Oversight; Lloyd Horwich, Policy Advisor for Subcommittee on Early Childhood, Elementary and Secondary Education; Lamont Ivey, Staff Assistant, Education; Thomas Kiley, Communications Director; Deborah Koolbeck, Policy Advisor for Subcommittee on Healthy Families; Ann-Frances Lambert, Administrative Assistant to Director of Education Policy; Danielle Lee, Press/Outreach Assistant; Ricardo Martinez, Policy Advisor for Subcommittee on Higher Education, Lifelong Learning and Competitiveness; Alex Nock, Deputy Staff Director; Joe Novotny, Chief Clerk; Lisette Partelow, Staff Assistant, Education; Rachel Racusen, Deputy Communications Director; Julie Radocchia, Education Policy Advisor; Michael Zola, Chief Investigative Counsel, Oversight; Mark Zuckerman, Staff Director; James Bergeron, Minority Deputy Director of Education and Human Services Policy; Robert Borden, Minority General Counsel; Kathryn Bruns, Minority Legislative Assistant; Taylor Hansen, Minority Legislative Assistant; Victor Klatt, Minority Staff Director; Susan Ross, Minority Director of Education and Human Resources Policy; and Linda Stevens, Minority Chief Clerk/Assistant to the General Counsel.

Chairman MILLER [presiding]. The Committee on Education and Labor will come to order for the purposes of holding a hearing on "Examining Unethical Practices in the Student Loan Industry." And a quorum being present, we will begin.

Good morning, and welcome to this morning's hearing on examining the unethical practices in the student loan industry.

Today we have asked the honorable Andrew M. Cuomo to provide an overview of his investigation into the egregious practices in the student loan industry and to share his thoughts on how we may address these issues at the federal level. It is our hope to continue to build on the good work of the attorney general.

This hearing comes at a time when it is getting harder and harder for our nation's students and families to afford college.

One of the major focuses of this Congress is how to help students and their families finance a college education.

We have already taken critical first steps to do just that by voting to cut interest rates in half on need-based federal student loans and by significantly raising the Pell grant scholarship funds available.

We also have introduced legislation to boost financial aid for students at no new cost to the taxpayers by making the federal student loan programs more efficient.

But as we work to make colleges more affordable, we also have the obligation to make sure that our nation's federal student loan programs are working as intended, to help students and families pay for college.

It has become extremely clear that these programs have been hijacked by third parties who are more interested in boosting their bottom lines than serving the best interests of students and families.

Between the conflicts of interest, the unethical practices revealed between lenders and schools, the improper use of the National Student Loan Database, to questionable stock holdings by public officials, we are talking about a system that is spinning out of control.

The blame rests not just with the lenders and the individuals who have exploited these programs but also with this administration.

Its failure to conduct proper oversight or to hold the industry accountable has harmed students and families, borrowers and taxpayers, all of whom ultimately pay the price for these corrupt practices.

Here in Congress, we have launched our own investigation into the student loan industry and their practices and the environment that has allowed this corruption to flourish.

We are closely examining the relationships and the conflicts of interest between the lenders, the financial aid officers, and public officials who are responsible for administering the student aid program.

And given just how little has been done to protect the students and their families from the abuse in this program, last week I called on the secretary of education to immediately take the following actions to eliminate the corruption and cronyism within the student loan industry.

I asked her to impose a moratorium on the use of preferred lender lists, to clearly define and end bribes paid by lenders, to require full disclosure by lenders and schools and their relationships, and to instruct schools and lenders to cease and desist all conflicts of

interest and to conduct oversight of the Department of Education employees.

I have called on the secretary to launch a public campaign to educate students and families about their rights and options when borrowing for college and to make public all records of loan industry meetings with political appointees so that the Congress and the American public can have a better understanding of who in the department has been lobbied by the industry.

There is no question that congressional action is urgently needed to put these programs back into the hands of students and parents.

Earlier this year, I introduced legislation called the Student Loan Sunshine Act that would clean up the relationship between lenders and schools.

My counterpart on the committee, Mr. McKeon, has also introduced legislation to address this problem. And soon, the committee will address these proposals to clean up this program.

I hope what we learn today helps us to build on these bills and to bring a sea change of reforms needed to this industry.

Ensuring that students and their families can have full confidence in our nation's student aid program is a critical part of our goal of making college more affordable and accessible.

Again, I want to thank our witness for joining us today and for the important work that he is doing on behalf of students and families in New York and across the country, for all of the contributions he has made to bring this problem to light and to encourage others to protect the students and families in their states to proceed in a manner in which he has to get these programs right side up and once again looking after the interests of students and their families.

And with that, I would like to recognize Mr. McKeon, the senior Republican on the committee.

[The prepared statement of Mr. Miller follows:]

**Prepared Statement of Hon. George Miller, Chairman, Committee on  
Education and Labor**

Good morning and welcome to this morning's hearing on examining unethical practices in the student loan industry.

Today, we have asked the Honorable Andrew M. Cuomo to provide an overview of his investigation into the egregious practices in the student loan industry, and to share his thoughts for how we may address these issues at the federal level. It is our hope to continue to build upon the good work of the Attorney General.

This hearing comes at a time when it's getting harder and harder for our nation's students and families to afford college.

One of the major focuses of this Congress is how to help students and families finance a college education. We have already taken critical first steps to do just that by voting to cut interest rates in half on need-based federal student loans, and by significantly raising the Pell Grant scholarship. We have also introduced legislation to boost financial aid for students—at no new cost to taxpayers—by making the federal student loan programs more efficient.

But as we work to make college more affordable, we also have an obligation to make sure that our nation's federal student loan programs are working as intended: to help students and families pay for college.

It has become extremely clear that these programs have been hijacked by third parties who are more interested in boosting their bottom lines than serving the best interests of students and families.

Between the conflicts of interest and unethical practices revealed between lenders and schools, the improper use of the National Student Loan Database, to questionable stock holdings by public officials, we are talking about a system that is spinning out of control.

The blame rests not just with the lenders and individuals who have exploited these programs for profit, but also on this administration.

Its failure to conduct proper oversight or hold the industry accountable has harmed student and family borrowers and taxpayers, all of whom ultimately pay the price for these corrupt practices.

Here in Congress we have launched our own investigation into the student loan industry and into the practices and environment that have allowed this corruption to flourish. We are closely examining the relationships and conflicts of interest between these lenders, financial aid officers, and the public officials who are responsible for administering federal student aid.

And given just how little has been done to protect student and families from the abuses in the program, last week I called on the Secretary of Education to immediately take the following actions to eliminate corruption and cronyism within the student loan industry:

- Impose a moratorium on “preferred lender lists;”
- Clearly define and end bribes paid by lenders;
- Require full disclosure by lenders and schools of their relationships;
- Instruct schools and lenders to cease and desist all conflicts of interest; and
- Conduct oversight of Department of Education employees.

I also called on the Secretary to launch a public campaign to educate students and families about their rights and options when borrowing for college, and make public all records of loan industry meetings with political appointees so that the Congress and the American public better understand who at the Department was being lobbied by the industry.

There is no question that congressional action is urgently needed to put these programs back in the hands of students and parents. Earlier this year I introduced legislation, the Student Loan Sunshine Act, that would clean up the relationships between lenders and schools. I hope that what we learn today helps us build on this bill to bring the sea change of reforms needed to this industry.

Ensuring that students and their families can have full confidence in our nation’s student aid system is a critical part of our goal of making college more affordable and accessible.

I again want to thank our witness for joining us today and for the important work he is doing on behalf of students and families in New York and across the country. We look forward to hearing his testimony.

Thank you.

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Mr. McKEON. Thank you, Mr. Chairman, for convening today’s hearing.

And to Mr. Cuomo, I thank you for joining us and welcome to our committee.

I don’t believe anyone would argue with the fact that trust in our student aid system has been shaken. That is why we are here this morning, after all.

So at the very outset of this hearing, I believe all of us can agree on a very basic yet vital goal for this hearing and the process that will follow it. And that should be to begin restoring that trust.

The question that we will face during the coming weeks and months will be how to meet that goal. There are a variety of reform proposals on the table already, here in Washington, in Mr. Cuomo’s state capital, and by organizations throughout the nation.

And I believe that is extraordinarily healthy, because this effort will require all stakeholders in the system to step up.

That means lenders, colleges, the Education Department, states and Congress all have a role to play. And where certain stakeholders don’t step up, this committee may be forced to step in.

Let me give you an example. Several years ago, when I served as chairman of the Higher Education Subcommittee, I urged financial aid administrators to work with other industry partners in adopting a series of recommended practices that would have helped deal with many aspects of the very situation we are presented with



this morning, such as a lack of disclosure for students and a lack of clarity with regard to preferred lender lists.

In short, they did not act quickly enough, and now it looks as if the committee is poised to do so.

If we do step in, Mr. Chairman, it should be for a very straightforward reason: to ensure this system continues to serve the needs of the students who depend on it for a chance at a college education.

This isn't about us versus the lenders or us versus the financial aid officers. This isn't about direct loans versus FFEL.

And for the record, I continue to strongly support the private-sector-based program and healthy competition between the government-run direct loan program and the private sector FFEL-based program.

No, this is about millions of young men and women who expect our student aid system to be there for them when they need it. By keeping our eyes fixed squarely on what best serves their need, we will be well on our way to restoring trust in the system.

With this in mind, earlier this week Mr. Keller and I introduced comprehensive legislation to address many of the issues which will be discussed at today's hearing.

The Financial Aid Accountability and Transparency Act builds on some of the recommendations you introduced earlier this year, Mr. Chairman.

Like your bill, we do not explicitly outlaw the practice of preferred lender lists. Rather, we reform this practice to ensure that it continues to serve the interests of students.

And like your bill, ours aims to protect against conflict of interest between lenders and financial aid officers.

However, our bill goes even further than those introduced by congressional Democrats.

For example, it asks colleges and universities to develop their own codes of conduct that must include restrictions on gifts, payments, stock and anything else that may give the appearance of a conflict of interest between financial aid officers and lenders.

Rather than simply requiring the reporting of it, our bill also bans revenue-sharing between lenders of private loans and colleges or universities. This practice already is illegal with regard to federal loans, and it is my view that it should be for private loans as well.

Instead of requiring even more lender and institutional reporting to the Department of Education, our bill requires extensive disclosure to students, particularly on matters relating to their financial aid rights, preferred lender lists and the like.

And finally, and perhaps most importantly, our bill explicitly allows an institution to negotiate lower interest rates or fees on loan products for their students and parents.

Why is this language in the bill, some may ask? Simply put, it benefits students. Mr. Keller and I would not propose restrictions that in any way short-circuit a student's ability to get a better deal.

With all of that said, Mr. Chairman, I believe that we can see a great deal of bipartisan cooperation on this issue during the coming weeks and months.

Despite some of the sensationalized press reports that have followed these investigations, we must not lose sight of the fact that the federal financial aid system must work for students and colleges alike.

We must be careful not to overreach as Congress does all too often. But we do need to restore trust in the system.

Once again, thank you, Mr. Chairman.

And, Mr. Cuomo, I look forward to your testimony.

[The prepared statement of Mr. McKeon follows:]

**Prepared Statement of Hon. Howard P. "Buck" McKeon, Senior Republican Member, Committee on Education and Labor**

Thank you, Mr. Chairman, for convening today's hearing. And to Mr. Cuomo, I thank you for joining us and welcome you to our Committee.

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The question that we will face during the coming weeks and months will be how to meet that goal. There are a variety of reform proposals on the table already—here in Washington, in Mr. Cuomo's state capital, and by organizations throughout the nation. And I believe that's extraordinarily healthy because this effort will require all stakeholders in the system to step up. That means lenders, colleges, the Education Department, states, and Congress all have a role to play. And, where certain stakeholders don't step up, this Committee may be forced to step in.

Let me give you an example:

Several years ago, when I served as Chairman of the higher education subcommittee, I urged financial aid administrators to work with other industry partners in adopting a series of recommended practices that would have helped deal with many aspects of the very situation we are presented with this morning, such as a lack of disclosure for students and a lack of clarity with regard to preferred lender lists. In short, they did not act quickly enough, and now, it looks as if this Committee is poised to do so.

If we do step in, Mr. Chairman, it should be for a very straightforward reason: to ensure this system continues to serve the needs of the students who depend on it for a chance at a college education. This isn't about us versus the lenders or us versus the financial aid officers. This isn't about direct loans versus FFEL—and for the record, I continue to strongly support the private sector based program and healthy competition between the government-run Direct Loan program and the private sector-based FFEL program.

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ents. "Why is this language in the bill?" some may ask. Simply put, it benefits students. Mr. Keller and I would not propose restrictions that in any way short-circuit a student's ability to get a better deal.

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Chairman MILLER. I thank the gentleman.

This morning in this hearing we have only one witness, and that is the honorable Andrew M. Cuomo.

Mr. Cuomo was elected the 64th attorney general of New York state on November 7, 2006. As attorney general, he is the highest-ranking law enforcement officer in the state, responsible for representing New York and its residents in legal matters.

The attorney general is no stranger to Washington, D.C., having served as secretary of housing and urban development under President Clinton. His work at HUD earned him the prestigious Innovation in American Government award from the Ford Foundation and the Kennedy School of Government at Harvard University on three separate occasions.

He is also no stranger to the lending institutions in this country and to the government-sponsored organizations that work with them.

In addition to his current work in the student loan industry, Mr. Cuomo is hard at work on protecting the people of the state of New York through investigations in nursing home abuses, drug trafficking and fraudulent practices.

We thank you, Mr. Cuomo, for your leadership on this issue and for the contribution that you have made to our understanding of that issue. And we look forward to your testimony. Welcome to the committee.

**STATEMENT OF HON. ANDREW M. CUOMO, ATTORNEY  
GENERAL, STATE OF NEW YORK**

Mr. CUOMO. Thank you very much, Mr. Chairman. And I thank the entire committee for the opportunity to appear before you today. It is a pleasure to be back before the Congress, albeit in a different position than my past positions.

I would also like the opportunity to introduce my deputy, Benjamin Lawsky, from the New York Attorney General's Office, who has been coordinating this case on college loans and is intimately familiar with our activity.

It is a pleasure to speak about this topic, and I want to begin by commending the chairman and Ranking Member McKeon for the good work that this committee has done on this issue.

I reviewed the legislative proposals. I think they go a long way toward remedying this problem, and it is a pleasure to be able to discuss it in detail today.

As you know, the magnitude of the problem is daunting. Two-thirds of all college students will leave school with a college loan. It is now an \$85 billion per year industry.

My office's investigation has found a wide range of improper and illegal activities occurring in a wide range of schools.

Bad practices occur at small schools with enrollments of less than 2,000 students and at large state universities with more than 20,000 students.

The problems exist across the country, from New York to California. There are a variety of troublesome activities that the schools and lenders have engaged in, many of which focus on the highly desirable preferred lender lists.

There are usually separate preferred lender lists for specific loans—Stafford loans, PLUS loans, private loans, et cetera.

In some instances, these preferred lender lists contain dozens of potential lenders. In other cases, the schools use the lists to recommend only a handful of lenders, sometimes a single lender.

The economic benefits to the lenders included on these preferred lists are powerful. Remarkably, 90 percent of students take their loans from the preferred list.

Why? Because the schools suggest these lenders to students, and students have trust in the schools.

When schools place lenders on the preferred list based on benefits to the schools as opposed to the students, the school violates that relationship of trust. In our opinion, this violation of trust makes a bad situation worse.

We have found a range of illegal activities, including direct payments to the schools as well as inducements to individual financial aid officers.

Aid officers are given expensive meals, travel to attractive locations, tickets to entertainment events, honoraria to serve on lender advisory boards.

In some instances, financial aid officers have even held stock in lending companies.

Benefits to the schools include lender-funded printing of schools' financial aid materials, lenders who are running call centers for the schools where the person who answers the telephone is identified to the student as a representative of the school even though it is actually an employee of the lender.

Another practice which we have found is "co-branding" between lenders and schools, using the school's colors, mascot and logos to convey at best the school's endorsement of the loan, and at worst a false impression that the loan is being offered by the school itself.

There are also disturbing practices with respect to opportunity loans, where a lender gives the school essentially a line of credit, sometimes offered in exchange for placement on the preferred lender list or for specified loan volume on other types of loans.

In my opinion, some tactics are a form of predatory lending. Allow me to quote from a lender's sales manual: "We leverage the school name as much as possible, because the target is already predisposed to the brand." The "target" is the student.

The most egregious practice that we have found is what is called revenue sharing. In revenue sharing arrangements, the lender pays the school a set percentage of the student loan volume.

The revenue-sharing arrangements are essentially undisclosed loan brokerage schemes, in my opinion, no better than illegal kick-back arrangements found in other industries.

These practices hurt students in at least two ways. First, the practices stifle competition. Closed lists mean less competition. Lenders who could actually bring down interest rates for student loans are often eliminated from the process.

Second, the lender payments and inducements increase the cost of the loan to the lender and are ultimately passed on to the students as the consumers.

In the case of the University of Pennsylvania, revenue sharing resulted in a \$500 added cost to each student taking the Citibank loans involved.

The good news is that as my office has exposed the illegal practices described above, consumers and the industry have heard the problems and they are responding.

Consumers are demanding reform and schools and lenders are willing to change course and set a new industry standard. To that end, we have entered into numerous settlement agreements with major lenders and schools in which they agree to adopt a new college code of conduct.

We have settled with Citibank and Sallie Mae, two of the nation's largest lenders.

Today we announced that we have reached agreement with Bank of America and J.P. Morgan Chase, the two main investors in the Sallie Mae private equity agreement.

We are pleased that both J.P. Morgan and Bank of America have separately agreed to our code of conduct, and I wish to applaud them for their cooperation and responsibility.

With these agreements, Mr. Chairman, the nation's top four student lenders have adopted our code of conduct. The code of conduct provides, in part, a total prohibition of revenue sharing.

It prohibits lenders from providing goods or services to schools in exchange for placement on the school's preferred lender list.

It prohibits lenders from making gifts or payments to school employees of more than nominal value.

It requires that schools recommend lenders to students only on the best interest of the students.

Finally, schools are prohibited from placing a lender on the preferred list for a particular type of loan in exchange for benefits provided to the school or the school's students in connection with different loans.

In sum, the code of conduct rights the wrongs our investigation has revealed. Our code and the House and Senate proposals are all on the same theory and seek the same goal.

I endorse Chairman Miller's Sunshine Act, which goes a long way toward ending the payments by lenders to school officials and requires important disclosures in connection with preferred lender lists.

The bill also extends disclosure obligations to the private side of the equation, an area which has been, to date, the Wild West of the student loan industry.

I would also point out that this issue resonates not only across the nation, Mr. Chairman, but also across the political aisle.

In fact, the legislation which I have submitted in my home state of New York has been endorsed by Republicans and Democrats alike.

In New York, every member of the state senate, a majority Republican body, has become a sponsor of the legislation. This is, indeed, a rare occurrence in New York's legislature. In fact, the state senate is poised to pass this legislation today.

In terms of the federal government's responsibility in this arena, let me say that having run a federal agency myself, I am not quick to criticize. However, I believe in this case the Department of Education has been asleep at the switch in at least three regards.

First, while there are Department of Education regulations governing conflicts of interest in the FFEL program, the safeguards were not extended to the private loan portfolio.

Over the last 5 years, private student loans have grown at an astounding average annual rate of 27 percent and now comprise 20 percent of all education borrowing. The business is huge, with the potential for abuse as the rates are not capped. It should not have been ignored.

Second, my investigation has shown that even where the Department of Education regulations did exist with respect to the FFEL program, there is significant evidence suggesting these regulations were flouted.

For example, Marist College in New York had a preferred lender list of four FFEL lenders, without disclosing that one of the lenders had an agreement to purchase the loans placed by the other lenders on the list.

The state university system of New York had a college which required students to pick a particular FFEL lender as their Stafford lender. This was a clear violation of federal law, under which a student is assured a choice of any lender.

The New York Institute of Technology chose FFEL preferred lenders by considering how much each lender contributed to sponsor the school's programs or events.

We have also found conflicted arrangements between Columbia University and FFEL lenders, where student financial aid officers obtained stock of one of the FFEL preferred lenders.

Third, it has recently been reported that the Department of Education rulemaking process, which was supposed to resolve these issues, has broken down.

To me, Mr. Chairman, that is like saying the fire truck has stalled on the way to the fire. It is simply unacceptable that the DOE can fail to right these wrongs in the midst of the disturbing revelations and at a time when students all across the nation are clamoring for guidance and help.

Announcing a task force at this late date is, frankly, too little, too late. The department can and should issue regulations immediately to affect reform in the industry and protect our students.

Today the marketplace is ahead of the regulators. Lenders and schools are reforming practices, and the Department of Education has still not acted.

Chairman Miller has written to the U.S. Education Secretary Margaret Spellings, calling on her to take emergency action to reform the nation's student loan programs, and I commend the chairman for his leadership on this issue.

I also commend Senator Kennedy for his outstanding leadership on this issue.

In conclusion, Mr. Chairman, I believe that real change is coming on this issue.

As Malcolm Gladwell explains in his book, *Tipping Point*, the awareness caused by these investigations has reached a critical mass that will demand response. The outrage resonates on many levels across the country, and change is under way from many sources.

Government is responding. Last week, over 40 attorney generals' offices participated in a conference call on this issue. State education offices are reforming practices. State legislatures are preparing legislative solutions.

Editorial boards are advocating reform. Significantly, the market itself is demanding a response, as students, now informed, are asking the tough questions, and lenders must change their practices or risk losing business.

Schools on their own initiative are changing their practices.

I believe in the states as laboratories of democracy, and I believe in the free market system to correct itself when the consumer is informed.

But I also believe that federal action is the swiftest, most comprehensive resolution to a nationwide injustice.

Change can and will come on this issue, Mr. Chairman. The question is how and when. It is not a time for just task forces or study groups. We know the facts painfully well. It is a time for action.

I look forward to federal leadership and cooperation, and I thank you and the committee for the honor of appearing before you today on this very important topic.

[The statement of Mr. Cuomo follows:]

**Prepared Statement of Hon. Andrew M. Cuomo, Attorney General, State of New York**

I thank Chairman Miller, Ranking Member McKeon, and the members of the Committee on Education and Labor for inviting me to speak this morning.

*Background*

Over the last few months my office has conducted an investigation into the student loan industry. In just the short time that the investigation has been ongoing, we have uncovered several significant, deceptive and illegal practices. Unfortunately, these practices are widespread throughout the country and throughout the many segments of the industry. These practices have affected hundreds of thousands of student borrowers and their parents.

It is easy to see why the results of this investigation have struck such a chord with the public. As the members of this Committee are well aware, the costs of higher education are soaring and have been for some time. Grant and scholarship funds have not kept pace with rising tuition. Accordingly, a significant and growing number of students and their parents turn to loans to cover what they otherwise could not afford. This is not just a problem in my state. Nationwide, two-thirds of all four year college graduates have loan debt. The student loan industry has swelled to become a greater than \$85 billion per year industry.

In spite of the large number of students and families that the student loan industry affects, the procedures of applying for and receiving loans are enormously complex and confusing. Students and their parents are faced with a dizzying array of loan possibilities and hundreds of potential lenders from which to choose.

These parents and students, not surprisingly, often look to the educational institutions they are attending for advice. They trust that the institutions will give them unbiased guidance as to how to best finance their education. In response, many institutions of higher education have created lists of recommended lenders. In some instances, these "preferred lender lists" contain dozens of lenders that meet certain minimal requirements. In other cases, educational institutions use the lists to rec-

commend a handful of lenders, or even a single lender, as “preferred.” The benefits to the lenders of being included on these lists are considerable. Lenders on preferred lender lists typically receive up to 90% of the loans borrowed by the institutions—students and parents. With this loan volume come vast profits for included lenders.

I am angered and saddened to say that our investigation has revealed an unholy alliance between lenders and many trusted institutions of higher education. The best interests of the lender and the institution, rather than the interests of the student, all too often have become paramount.

I will take the next few minutes to elaborate on a few of the troubling, deceptive and often illegal practices that we have uncovered.

#### *Problems Uncovered*

##### *Revenue Sharing*

What I believe to be the most egregious practice that we have uncovered so far is a form of kick-back scheme often referred to as “revenue sharing.” Revenue sharing is an arrangement under which a lender pays an institution of higher education a percentage of the principal of each loan taken out by a borrower at the institution. The practice of revenue sharing creates a potential conflict of interest on the part of the institutions of higher education. When and if the institutions direct students to lenders, the direction should be based solely on the best interests of the student and parents who may take out loans from the lenders. Because of these revenue sharing arrangements, however, the institutions have a financial interest in the student or parents selecting the revenue sharing lender, regardless of whether that lender offers the best rates and service for that borrower. The advice the students and parents sought from a trusted source may not be so impartial after all.

##### *Preferred Lender Lists*

As I mentioned before, many schools maintain preferred lender lists and encourage students to borrow from the lenders whose names appear on the lists. Despite the significant role that these lists play in determining the lenders from which students and parents borrow, many institutions have chosen not to inform their student and parent borrowers about the criteria used to formulate the lists of recommended or preferred lenders. In some instances, they have even gone so far as to actively conceal the methods by which their recommendations derive. Worse, some institutions fail to disclose the potential and all too often actual conflicts of interest on the part of their financial aid offices—the same offices which compile the preferred lender lists. These conflicts of interest may arise from the revenue sharing arrangements I just described or from other perks or consideration granted to schools and financial aid employees, some examples of which I will describe in greater detail.

##### *Improper Relationships Between Lenders and Financial Aid Offices and Administrators*

Our investigation has uncovered potential conflicts of interest created by financial aid administrators who have held stock in a lender, having been encouraged to purchase the stock by a lender executive. In other cases, financial aid administrators have received payment for consulting with a lender. In several of these cases, the implicated lenders succeeded in getting themselves placed on the implicated administrators’ schools’ preferred lender lists.

Not all of the improper perks have been so egregious, but many have been exceptionally widespread. Many lenders have paid travel expenses and honoraria for financial aid officials to attend meetings and seminars in attractive locations often as part of an appointment of the institutions’ financial aid officials to “advisory boards” or “committees” sponsored by the lenders.

We have also uncovered many examples of lenders paying hundreds of thousands of dollars for printing services at the request of financial aid officers. Some lenders have also sent their own staff to assist schools’ financial aid staff on the schools’ campus. The lenders did not offer these services out of the goodness of their hearts. Similar to the revenue sharing arrangements, lenders granted institutions of higher education these types of benefits in an effort to encourage the institutions to steer students to the lenders.

In a related problem, lenders have agreed with institutions of higher education to staff “call centers” that answer students’ telephoned or emailed questions regarding financial aid, loans and lenders. Often the call center employees have not only failed to identify themselves as employees of a lender, but have been instructed to answer the phone in the institutions’ name. The student calling or emails their questions rightfully expected to receive disinterested advice and information regard-



ing lenders. These lender call center employees, however, have an interest in advocating on behalf of the lender that pays them.

#### *Denial of Choice of Lender*

Our investigation has also brought to light a failure of some institutions of higher education to make clear that borrowers have a right to select the lender of their choice, irrespective of whether the lender appears on any preferred lender lists. In the most egregious cases, institutions have gone so far as to abrogate this right, by stating or strongly implying that the student and parents were limited to the lenders on the list, or even to a single lender. In this way the educational institutions steer borrowers to certain lenders, as with the other examples, not necessarily because that lender is best for the borrower.

#### *Undisclosed Sales of Loans to Another Lender*

Further, in many instances, institutions of higher education place several lenders on the institutions' lists of preferred lenders causing the potential borrower to think that the lender list represents a real choice of options. However, the choice is illusory when, as sometimes occurs, all or a number of the lenders on a lender list have arranged with each other to sell any loans to one of the lenders immediately after one of the other complicit lenders disburses a loan.

#### *Quid Pro Quo (Opportunity Loans)*

Deeply disturbing, too, was our discovery that lenders and colleges had, in many instances, entered into quid pro quo high risk, high interest loans that hurt students. Under these undisclosed agreements, often referred to as "opportunity loans programs" lenders agreed to make loans up to a specified aggregate amount to students with poor or no credit history, or international students, who the lender claimed would otherwise not be eligible for the lender's alternative loan program. In exchange for the lender's commitment to make such loans, however, the institution provided concessions or promises that prejudice other borrowers.

#### *Solutions*

##### *Code of Conduct*

Over the last few weeks, as my office exposed many of these practices to the light of day, I was pleased to see many lenders and schools that had engaged in some of the questionable and even illegal practices agree to change course and set a new standard for the industry. To that end, we have entered into numerous settlement agreements—with major lenders and schools alike—in which the schools and lenders agreed to adopt a new landmark Education Loan Code of Conduct, which will now govern those institutions' student loan practices going forward. The Code of Conduct offers institutions the guidelines many schools and lenders have actively sought and by which all schools and lenders should be willing to abide.

The Code of Conduct remedies the troubling and illegal practices we have uncovered. Specifically, the Code of Conduct prohibits revenue sharing and kickbacks in other forms, including printing services. It prohibits lenders from funding gifts and trips for institutions' financial aid employees. The Code prohibits lender staffed call centers. Our Code also lays out strong but fair guidelines concerning, among other things, preferred lender lists, advisory board compensation, and loan resale.

My office will continue to pursue lenders, schools, and other players in the student loan industry that fail to put students' interests first. In cases where the law has been broken, we will continue to demand that the responsible entity agree to cease the illegal practices, reimburse wronged borrowers or pay into our education fund as appropriate, and agree to abide by the Code of Conduct. If not, we will sue.

##### *State Legislation*

But, to most effectively reform the student loan industry—and to restore most fully the broken trust between universities and lenders on the one hand and students on the other—legislation is necessary so that these types of reforms come to all lenders and schools. I respectfully submit that it is crucial that Congress act promptly to end the conflicts, perks and revenue sharing that have been costing our students dearly. I ask you to move quickly to ensure that, as another group of high schools students look toward beginning their college educations in the fall, we have reform in place that will keep the students' interests paramount.

That is why I was so pleased to stand on April 16 alongside my state's legislative leadership when we announced the introduction of state legislation that will codify and lend additional enforcement strength to the Code of Conduct. Our legislation addresses, on an industry-wide basis, the problems exposed as a result of my office's ongoing investigation into the widespread conflicts of interest throughout the student loan industry.

*National Action*

The settlements into which we have entered in New York will affect millions of students and thousands of schools around the country. Recently, my office has entered into settlements involving other states' attorneys general. Most notably because of the leadership of Illinois Attorney General Lisa Madigan and Missouri Attorney General Jay Nixon, we have been able to broaden the impact of our investigation by entering into settlements with multiple states simultaneously. The legislation we have proposed in New York will continue the reforms we began through our investigation and I hope other states will follow suit. We have certainly taken a major step in cleaning up a system laden with conflicts of interest.

*Congressional Action Needed*

Yet there is much more that needs to be done—and we must move without delay. That is where this Congress can play a significant role.

Part of the reason the practices we have uncovered have been able to flourish nationwide over the past several years is because the U.S. Department of Education has been asleep at the switch. The practices we have uncovered were not undiscoverable until now. Rather, the entity charged with maintaining the integrity of the student loan market failed. The failure of the Department to pass adequate regulations is disappointing and irresponsible.

Now is the time for Congress to act to affect change in this industry; an industry that until very recently has functioned without proper oversight. Congressman Miller and Senator Kennedy have both been extraordinary leaders on this issue for years. I believe that Chairman Miller's Student Loan Sunshine Act will go a long way toward bringing the much needed disinfectant of sunlight to this tainted industry. I would encourage the Committee to ensure that the bill is ultimately brought to the floor of the House soon.

*Conclusion*

In closing, I urge Congress to enact the Student Loan Sunshine Act. Further, this Congress must ensure that the trust placed in educational institutions is warranted and that we end the pernicious effects of financial gain through the misleading of students and their families. The stakes are too high for too many Americans' futures for Congress not to act. I look forward to providing any assistance the Committee may require of my office to help achieve these goals.

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Chairman MILLER. Thank you very much, General Cuomo. Again, we appreciate all that you have done and certainly taking the time to come here and to brief the committee on this.

I think given your remarks and the remarks of Mr. McKeon and hopefully my own—we will be able to achieve that kind of bipartisan consensus on our legislation out of this committee that apparently you were able to achieve in the New York legislature, which is no easy trick, as we know.

And we hope to be able to continue to work with you as we develop that legislation to make sure that we are, in fact, addressing it based upon the evidence that you have from your investigations.

You mentioned the shared revenues, the preferred lender list, and maybe even the agreement—well, the preferred lender list and that it was sold originally as a convenience to students and their families, and it has been corrupted to be for the convenience of the universities and the lenders.

But you also in your testimony and in your actions already have secured rebates to those students that starts to quantify the real cost of these corrupt practices on students and their families as they struggle with the cost of college.

We have heard in this committee, and we have certainly heard in our districts, where students or families will talk about having to spend \$100, \$200, \$250 for textbooks and that may be a make or break item for the question of whether or not they are going to

go to college that semester or go to work and then go to college the next semester.

You are talking about \$500 rebates. Do you want to expand on what you might think the real cost here is?

You know, this isn't just a matter of convenience and friends working with one another over the years. This money comes out of the subsidies that are provided by this government to the lenders.

Mr. CUOMO. Well, Mr. Chairman, I totally agree, and you are very correct on the point. These are significant economic benefits. We are not talking about loose change here. At some schools, it is in excess of \$1 million per year, the amount which is "revenue sharing."

Revenue sharing is basically a commission that the school gets for referring business to a particular lender. Undisclosed, the school will come to an arrangement. The lender gets on the "preferred list."

The lender wants as small a list as possible. From the lender's point of view, ideally, they would like to be the only preferred lender. The students trust the school's recommendation. Ninety percent of the students wind up taking the preferred lender.

More business for the lender, and the schools get revenue sharing, basically a commission on the volume that goes to the lender.

And it can be easily in excess of \$1 million per year for the school. What does that mean to the student? What I mentioned in the testimony—in the case of the University of Pennsylvania, which is a case that we have handled and we have settled, so I am free to discuss it at this point—when the University of Pennsylvania, as part of the settlement, had to return that money to the students affected in that year, it is roughly \$500 per student.

And \$500 per student is a lot of money, especially with the cost of college and all the financial pressures that are on these students.

Chairman MILLER. When you have the preferred lender program—and again, you know all of the iterations that are out there, and you have looked at them—do we know whether or not those preferred lenders—or in one case, you describe where they whittled it down to one lender with four other entities cooperating with the single lender.

Do we know whether or not, in fact, those were the low-cost lender that was available at that time to the students?

Mr. CUOMO. You don't know, Mr. Chairman, because often the decision on the preferred lender is the lender preferred by the school as opposed to the lender preferred because it is in the best interest of the student.

Why would a school prefer a lender? Because they have a revenue-sharing agreement, or it was the most productive revenue-sharing agreement, or because the lender is providing employees, or because the lender is favored by the financial aid officer in the school who might own stock in that lender, or maybe went to a conference, or maybe he has gotten gifts.

So the school prefers the lender, and that preferred lender is on the list. The students then trust the school's opinion and advice and take that lender.

If you really had an open system, and you really had competition, and you were really competing for the rates, then we would know who the best lender was for the students. But all too often that is not the decision and it is not the criteria.

Chairman MILLER. My time is about to expire. What contact or what discussions have you or your staff had with the Department of Education as this investigation of yours has evolved?

Mr. CUOMO. Mr. Lawskey can provide more specific information, but we have been in touch with the department. We have shared information with the department. And as cooperative or as helpful as we can be in sharing our findings, it would be our pleasure.

Chairman MILLER. So we can assume, therefore, that the Department is not just reading about this in the paper and moving along at that speed, that they—

Mr. CUOMO. I believe there has been—

Chairman MILLER [continuing]. Have been informed of the investigation and some of the problems that you have encountered and some of the practices you have encountered.

Mr. CUOMO. Yes, they have, Mr. Chairman.

Chairman MILLER. I share your concerns about the department. I don't understand their slowness to react to this situation, and I stated—and they haven't agreed to them, the five things that I thought they should do immediately to strengthen this program and end some of these practices.

We are in contact with the secretary, and we are in the process of negotiating with her and her office for an appearance before this committee, hopefully within the next 2 weeks.

My time has expired. Again, thank you very much, General Cuomo.

Mr. McKeon?

Mr. McKEON. Thank you, Mr. Chairman.

And thank you, Attorney General Cuomo, for your testimony and for the work that you are doing.

One thing that I hope we leave this hearing with is the idea that not all federal aid administrators on the campus are picking preferred lenders or are acting in interests that are not the best for the students.

We have over 6,000 schools participating in this program, and I think we don't want to paint with a broad brush the fact that all of these people are doing some of the things that have been mentioned. I think that that really is not a reasonable assumption.

And we have about 3,500 lenders, and I don't think we want to leave the assumption that all of them are doing things that would violate the standards that we have been talking about.

Mr. Cuomo, I understand that you have contacted Clemson University about an arrangement that they have with an alternative loan lender.

I have a letter from the South Carolina Attorney General's Office that I would like to enter into the record, if I may, Mr. Chairman.

Chairman MILLER. If there is no objection—hearing none, so ordered.

[The information follows:]

OFFICE OF THE ATTORNEY GENERAL,  
STATE OF SOUTH CAROLINA,  
Columbia, SC, April 10, 2007.

ZACHARY STURGES, *Esquire*,  
Assistant Attorney General, Investment Protection Bureau, Office of Attorney General  
Andrew Cuomo, New York, NY.

*Re: Proposed Agreement on Code of Conduct with Clemson University*

DEAR MR. STURGES: This letter is a follow-up to your discussions with Clemson University and this office concerning Clemson entering into a Code of Conduct Agreement with the New York Attorney General's Office as to the practices related to higher education loans offered to students and parents. Specifically, your interest was in the area of private "alternative loans" that may be promoted by a university, such as Clemson, with preferred lenders in which there is a revenue sharing agreement. As you are aware, Clemson has one such arrangement with Education Finance Partners, Inc. (EFP) which was entered into in April 2006 after EFP was selected pursuant to Clemson following the State Procurement procedures.

Pursuant to your inquiry, this office, in conjunction with Clemson University, has reviewed Clemson's practices with regard to student financial aid, including the practices addressed in your Agreement. Based upon this review, we confirm herein what we orally advised you yesterday—that Clemson will not be entering into the Agreement. This decision was based upon our determination that as to student financial aid, generally, and preferred loans with revenue sharing agreements, specifically, no conflicts of interest existed and no untoward relationships are present.

We appreciate your office's work and interest in the area of the relationships between colleges and lenders as to student financial aid. Based upon our discussions with you, Clemson, in conjunction with consulting with this office, will continue to monitor its student financial aid program, including whether or not to continue with its preferred lending-revenue sharing arrangement. Further, based upon discussions with your office, Clemson has added language to its loan program website which is already included in the "Federal Truth in Lending Disclosure Statement" that provides additional notice of the revenue sharing arrangement. Also, as you have been advised, Clemson will continue to use any revenue generated pursuant to this arrangement to fund a program for emergency funds for students. Clemson is proud of its reputation as being one of the finest public institutions in the country and its goal is to continue that recognition in the area of student loan programs.

Once again, Clemson and this office thank you for your time and consideration in discussing the issues in this matter. We also appreciate the benefit of your expertise and your sharing with us the results of your investigation. Personally, I have enjoyed working with your office in the areas of antitrust and consumer protection and look forward to working with you and your office in mutual areas of concern in the future.

Very truly yours,

C. HAVIRD JONES, JR.,  
Senior Assistant Attorney General.

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Mr. McKEON. This letter says it has examined——

Chairman MILLER. General, do you have a copy of this?

Mr. McKEON. Very expeditious. It says here that they have examined the situation between Clemson and the lender, and they don't see any impropriety with the relationship and will not be taking any immediate action.

Will you be filing a lawsuit against Clemson?

Mr. CUOMO. Congressman, the attorney general wears two hats, at least, in this regard—any attorney general. Number one, you protect the people of your state from a consumer protection point of view, and number two, you are also the counsel for state agencies, state universities.

And in the case you point to, the attorney general is defending the university. In my state, we also serve as counsel to the university system. And the matter is ongoing. We are looking at it.

And we will be looking at the facts on the case and speaking to the attorney general, speaking to the school. Wherever we can come to an amicable resolution, that is our preference.

We have come to voluntary agreements with over 16 schools and four of the nation's top lenders, all on a voluntary basis. So to the extent we can resolve differences amicably, that is always my preference.

Mr. McKEON. I would agree with that. And as you mentioned, as the attorney general for the state of New York, I assume that you are counsel for all state institutions, because that is the way most states function.

I, like most people, assumed that colleges already had strong conflict of interest policies in place. As a counsel to state colleges or in discussions with other college counsels, do you know why they did not have strong conflict of interest policies in place in your particular state?

Mr. CUOMO. Well, Congressman, I think your first point is correct. This is not to say that all colleges or all lenders have been engaging in this type of behavior. I agree with you.

Mr. McKEON. Probably the vast majority, I think we would agree.

Mr. CUOMO. That is exactly right. We are trying to restore the integrity and confidence and trust in the system.

And to do that, I believe we need to put the reforms in place so we can say to every student on every campus, "Don't worry, we have resolved this issue," because as your point is well taken, it is not every school, from a student's point of view, if it is only their school, that is enough of a problem. And that is why I think we need industry-wide reforms.

Many schools do have conflict of interest resolutions and a code of conduct for their employees. Many state university systems do have an additional code of ethics on top of the normal college code of ethics.

So many of the schools do. Some don't. Some cases we have come across, the employee was in violation not of just the law but also the code of ethics for that college. So there are a variety of situations.

Mr. McKEON. Just having codes doesn't necessarily mean—

Mr. CUOMO. That is exactly right. It is also the policing. It is also the oversight.

Mr. McKEON. Thank you, Mr. Chairman. My time has expired. Chairman MILLER. Thank you.

Mr. Payne?

Mr. PAYNE. Thank you very much.

Let me commend you, Mr. Cuomo, for the outstanding job you have done at highlighting this and bringing attention to it.

You know, my colleague just mentioned—of course, being a former—had mentioned that colleges tend to have strong codes of conduct.

And you know, I am not so sure that we can simply make a blanket statement of that nature, when I look at the credit card situation that goes on in colleges.

You talk about bad practices. And I hope you would take that on. So I am wondering where all this code of conduct is coming from administrators of colleges.

Kids are sent credit cards. They are 18 years and 17 years and 19 years old, never had an opportunity to have any economic freedom, because they don't have—they haven't earned it.

And that is why when these cards come through, encouraged by the colleges, booths set up at colleges, college employees calling students—I mean, what kind of code of conduct—where is the code of conduct?

You know, in my district, they did a big investigation on, guess what, the Earned Income Tax Credit people. Now, anybody that breaks the law is wrong. Earned Income Tax Credit recipients mean people made between \$13,000 and \$28,000 a year.

And they went through all of these audits to see whether these \$13,000 to \$28,000-a-year people were honest about what they were putting down. Did they get food stamps and didn't put it on?

Here, you have got people—and you use nice words like revenue sharing and preferred lenders. If this was anywhere else, people—I haven't heard anybody talking about subpoenas, putting somebody's hand up to see whether they have broken a law or not.

And you know, you are the messenger. I am just simply saying that when it comes to the white collar people, we tend to have fancy names. We tend to let students continually get the shaft. And people walk away willy-nilly on these issues.

When it comes to the guy who is struggling and grunting and makes a mistake, they lay the book on him, you know?

What is going to happen? What about the credit card business? What is going to happen to these people who are taking kickbacks? That is what they would say in my neighborhood. It is a kickback. Kickbacks are criminal. They go to jail. They pay fines.

What is it going to be? Is this going to be some, "Well, we have new reforms and that is good?" What about what has happened already—students who have struggled to pay their way through, still have loans, and guys are buying bigger cars?

Mr. CUOMO. Well, Mr. Congressman, I agree with the sentiment and the points you have raised. In my testimony, I said that I believe these are kickbacks. We have issued subpoenas.

And I believe this is illegal activity, make no mistake about it. I believe it violates consumer protection laws. I believe it violates business law.

And you are right, it is offensive. I believe it is especially offensive because schools are in a relationship of trust. This is not a normal marketplace relationship.

This is not a relationship of caveat emptor, let the buyer beware. This is a student going to the school. Ninety percent of the students are following the school's recommendation because there is a relationship of trust.

These are incoming students. They want to be part of the school. The school says, "Go to this lender." They go to that lender.

And then to find out that there was a different relationship or another relationship, or there was a "kickback" that was undisclosed—I think it is illegal. It is wrong. It is offensive. It is unethical. It is improper. We are going to enforce the law.

The question that I was trying to respond to in my testimony is, "And what is the response of the federal government at this time? What is the response of the Department of Education?"

We have laid out the facts. In my opinion, we don't need another task force or a study group. We know the facts painfully well. We have done the subpoenas.

We have schools all across the country. We have states responding. We have attorney generals responding. Schools themselves are responding. Four of the top lenders in the country have responded.

And now what is the federal government going to do? And what is the Department of Education going to go? That is the question that I am focused on today.

But rest assured, Congressman, for the state of New York, we are working cooperatively with the attorney general from New Jersey. We will enforce the law, and we will do what we can as state officials.

But I think it is a tremendous opportunity for the federal government to come in and really resolve this injustice nationwide.

Chairman MILLER. The gentleman's time has expired.

Mr. Keller?

Mr. KELLER. Thank you, Mr. Chairman.

And thank you, Mr. Cuomo, for agreeing to be here today. I am especially troubled about hearing of the conflict of interest that exists where financial aid administrators receive consulting fees or stock from lenders. We have common ground in our belief that this is wrong and unacceptable.

Now, your investigation, I believe, has focused primarily on the private alternative loan market and not the federal student loans such as the Stafford loans, which are guaranteed by the federal government under Title IV of the Higher Education Act. Am I correct?

Mr. CUOMO. You are correct.

Mr. KELLER. Did your investigation reveal any specific problems with the federal student loan program that resulted in any students paying either a higher interest than the law allows or higher origination fees than the law allows?

Mr. CUOMO. Well, Congressman, two points. First, we have focused on the private loans because that is the growing area of the market. There are no caps in that area of the market. And it is virtually unregulated, so we have been focusing on the private loans.

We have also come across instances in the FFEL program where there are activities in violation of the regulations that cover the FFEL program.

I spoke about Marist College, which in our opinion violated regulations of the FFEL program—Columbia University, New York Institute of Technology.

Mr. KELLER. And I don't want to cut you off, but I heard you testify, and I wrote your notes. I know you think there is some violations of FFEL. I am getting to did you ever see any instance where a student was hurt for paying like a higher interest rate.

For example, the interest rate now is 6.8 percent as of July. Did you in your investigation see something where the student is paying 7.5 percent or something to that effect, where the student was actually financially hurt?



Mr. CUOMO. Well, Congressman, as you know, the rate is capped under the FFEL program, but the concept that justifies the FFEL program, or the best case for the FFEL program, is, "Well, we are going to have competition among private lenders."

And the competition among the private lenders might bring the interest rate down, or there might be a discount on the back end.

If you have a preferred lender list and preferences for the schools, you never get to competition, so you don't really know if you got the best loan for the students, since the lender was selected in the interest of the school rather than the interest of the student.

Mr. KELLER. I hear you. And you found an instance where they only got one choice under the FFEL program and you were concerned about that, correct?

Mr. CUOMO. Yes.

Mr. KELLER. Okay. Now, the main federal student loan program is Stafford, and one out of five students get their Stafford loans direct from the federal government. Four out of five get their loans under the FFEL program from private lenders.

Senator Kennedy, Chairman Miller, former President Clinton have all indicated their preference for the direct loan program. Do you prefer the direct lending program over the private FFEL program?

Mr. CUOMO. I understand the arguments for both, and I understand the argument that in the FFEL program you could have a situation where competition brings down the cost of the loan.

I don't believe that is what is occurring, but I understand the concept and the theory.

The direct program, obviously, has benefits, that the federal government directly is making the loan, you don't have a private lender and you have reduced costs.

So I understand the arguments for both. I am not here as a policy official today. At one time, I appeared before Congress as a Cabinet secretary where I made policy cases and defended policy.

Now I am just a law enforcement official and speaking about the findings of our investigation.

Mr. KELLER. All right. Mr. Cuomo, the reason I asked you that—because when you leave here, and all the smoke is cleared, I am going to hear from some people on the other side of the aisle saying, "Hey, we had the attorney general from New York here. He talked about a few bad apples in the private lending program. We have got to do away with private lending on the federal level and switch to direct student lending."

And so when I hear that argument, I just want to go back and say to them, "We had Attorney General Cuomo right here, and he didn't express that opinion." Is that a fair thing for me to say?

Mr. CUOMO. You can say he is not a policy maker; the attorney general was just here talking about the facts from his investigations.

Mr. KELLER. All right. As a non-policy maker, let me ask you this, Attorney General. You have testified that the U.S. Department of Education has been asleep at the switch, it is irresponsible, and it has failed to maintain integrity.

If that is the case, why should we put the Department of Education in charge of all of the federal student loans?

Mr. CUOMO. I believe the Department of Education in this situation—again, my focus here is narrow and specific to the situation at hand on college loans and the findings from my investigations, and my work with schools all across the country and attorneys general all across the country.

I think the Department of Education should have—retrospectively and prospectively should be doing a better job on oversight of the FFEL program.

I believe that the Department of Education's oversight should be extended to the private loan program. That is an area that is growing. That is the area where we have evidence of abuse. That is the area where, by design, you have the proclivity for abuse. I believe that also.

I also believe the Department of Education should be faster and more aggressive in issuing regulations on the activity that we have found.

There is a tremendous amount of information available to this committee and to the department. We have numerous cases all across the country. The marketplace is responding. Schools are changing. Lenders are changing.

The federal government is in the oversight capacity, and I believe the Department of Education should be more aggressive in promulgating regulations that address this issue today.

Mr. KELLER. Thank you, and my time has expired.

Mr. CUOMO. Thank you, sir.

Chairman MILLER. I find it interesting that the direct loan program in the eyes of my colleagues, some of them on the other side of the aisle—that it can't compete, and yet the private lenders went in and paid the University of Indiana \$3 million to drop the direct loan program, so apparently they thought it could compete if it was left to its own.

Mr. Andrews?

Mr. ANDREWS. Thank you, Mr. Chairman.

Thank you, General, for your testimony here this morning.

Mr. Chairman, I look forward to supporting your legislation. I think it is very timely. I wish it weren't necessary. I wish the Secretary of Education had been more proactive and aggressive in responding to your requests just a few days ago.

General, you say you are not a policy maker. You may not have made policy, but you made a lot of sense and made a lot of progress already, and we thank you for that.

Mr. CUOMO. Thank you.

Mr. ANDREWS. You have certainly recovered substantial amounts of money for students. That is to be commended. You have induced responsible members of the lending community to take their own initiative and clear up this problem, for which we thank you. And you have opened up a very important debate.

I wanted to ask you some questions about how we might build on your work and prevent this sort of thing from happening in the future.

With respect to the cases that have already settled, so there is no litigation strategy you have to disclose, how did you derive the numbers of the settlements that you agreed to from the universities with which you settled?

Mr. CUOMO. Thank you, Congressman, for the question. There are two basic scenarios.

For schools that received payments from lenders that we believed should not have been received in the first place, and where the amount of money made it practicable, the school returned the money that it received from the lender to the students who took those loans from that lender in that year.

Mr. ANDREWS. So these were the preferred payments. The revenue-sharing payments were returned.

Mr. CUOMO. Yes. So if a school received payments from a lender, under our statements the school gave that amount of money to the students who took the loans, because my basic point was that was a cost of the loan.

If the bank had to make a payment to the school, that was a cost of the loan. If the bank wasn't making that payment to the school, they could have reduced the cost to the student, so the school should give the money to the student.

The case we discussed, University of Pennsylvania—that came out to about \$500 per student.

In situations where the students have already been compensated, or the amount of money just doesn't make sense from a practical point of view to distribute to the student body, we have also set up an education fund where we will run a program to educate high school students about loans and their parents about the available loans and the best way to get a loan.

And some schools or lenders are contributing to that fund.

Mr. ANDREWS. Do you think that the harms that you helped to remedy here would have been avoided if we had a statutory requirement that schools make available on a level playing field basis—the same Web site, the same booklet, whatever—every private lender that is out there that might bid on the student's business?

If we opened this up and said, "Look, if you are going to refer information about one lender, private lender, you have got to refer information about all of them that wish to be in the marketplace," would that work?

Mr. CUOMO. Yes, Congressman. I think the point of getting—breaking the monopoly of the preferred lender list—you have to break that monopoly.

And that list or those recommendations must be regulated to the point that the decisions are being made based on the best interest of the students without any conflict of interest and not in the best interest of the school.

I am not against preferred lender lists. There are a lot of lenders out there, and it is very confusing.

And if a school wants to provide a service of doing the due diligence, and doing the review, and coming up with one or two or three or four lenders they want to recommend to the students, because they honestly believe it is in the best interest of the students, and they have done their homework, and they say, "They have the best rates, and they have done the best servicing, and we have a good relationship," fine.

Mr. ANDREWS. So if we had some fair and open process based upon criteria of merit, where everyone who passed the merit could

be listed on a Web site or put in a booklet, and then the student could choose among those competing lenders, do you think that would remedy the situation?

Mr. CUOMO. Yes. And I think there are two sides to the equation. Number one, the school has to be making the determination in the best interest of the student. That should be the criteria, not what is good for the school, what is good for the student.

Second, there can't be any other relationships that would pose a conflict of interest. You can't be a financial aid officer that is exercising discretion but you are also on the advisory board of the bank.

Mr. ANDREWS. Right. Frankly, there is a pattern for this in other areas of our jurisdiction in labor law, where labor union officials are not permitted to take any kind of compensation from the employers from whom they are negotiating in order to preserve their objectivity. Something like that would probably work.

Mr. CUOMO. That is exactly right. That is exactly right. It is done in many other areas.

And I frankly think, Congressman, there is an opportunity for the federal government here, because as Congressman McKeon pointed out, we need to restore consumer confidence here. Students are nervous. Students are asking questions.

The industry needs to restore consumer confidence. The lenders, the schools, the guarantors—they want to restore consumer confidence.

Let the federal government lead the way, pass the regulations, improve the oversight and restore the confidence of the industry. That is in everyone's best interest.

Mr. ANDREWS. Thank you very much.

Chairman MILLER. The gentleman's time has expired.

Mr. Petri?

Mr. PETRI. Thank you, Mr. Chairman.

Thank you, General, for your testimony today. Can you tell me if you found any examples of abuse or questionable behavior in the direct loan program, or are all the instances of these questionable transactions and so on in either the private market or FFEL program?

Mr. CUOMO. Off the top of my head, Congressman, I don't know of any cases we brought in the direct loan arena. I mentioned the ones in the FFEL program, and we were primarily focused on the private loans.

Mr. PETRI. Now, some years ago, when the man you worked for over at the housing department was leading in this area, we had 50 percent direct loan and 50 percent, about, of the guarantee program.

Now it is about 80-20. President Bush and his Office of Management and Budget indicates that the direct loan program costs about one-third as much as the guarantee program to the taxpayers.

Do you think the concerns of the taxpayers, if the terms are equal to students, should be a factor in schools combining preferred lender lists and this sort of thing?

Mr. CUOMO. Congressman, I don't think we have to choose between the interests of the taxpayers and the interest of the students.

Mr. PETRI. No, but what about the interest of the schools? It is not a question of students and taxpayers.

It is a question of direct and indirect, and the guarantee program, indirect program, costs the taxpayer three times as much, according to our Office of Management and Budget, as the direct program.

And the direct program has none of these ethical problems that you have been mentioning, as best—according to your testimony, at least.

So why wouldn't we ask that they put the direct program on any preferred lender list that they decide to do, since the terms are the same? At least the direct program certainly is not any higher than these guarantee programs.

Mr. CUOMO. Well, no, Congressman, I agree. The direct program has significant benefits. And the rates are the same between the direct program and the so-called FFEL program, but there is no private lender involved, so there are just fewer transactions, fewer connections.

And we have not come across any cases in the direct loan program, but again, our focus was on the private loan program. We found instances in the FFEL program. We didn't find instances in the direct loan program.

Mr. PETRI. Now, there are a lot of schools that have stayed with the direct loan program—my state, Marquette University, Harvard University, Michigan and Minnesota.

And yet we have seen the guarantee program go, despite that, from maybe 50 percent of the loans up to 80 percent of the loans.

Why would you think schools have chosen to engage in transactions with private lenders—

Chairman MILLER. Would the gentleman yield, Mr. Petri?

Mr. PETRI. Will there be another round?

Chairman MILLER. Okay.

Mr. CUOMO. Quickly, first, lenders work very hard, obviously, to insert their product through the FFEL, the guarantee program, rather than the direct program. And the industry is effective. And there are significant incentives offered to schools to drop out of the direct program and take the guarantee program.

Mr. PETRI. So you don't think there is actually a fair competition between the direct and the guarantee program in the marketplace today, and that might account for this?

Mr. CUOMO. I think that is correct.

Mr. PETRI. Thank you.

Mr. McKEON. Again, you have just a second left. Just to clarify the record, as far as I know, the direct lending got up to about 39 percent. I would just like to have it clarified in the record whether it is 50 percent or 39 percent.

I believe it is closer to 39 percent, just for the record.\*

Chairman MILLER. We will get that for the record.

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\*Loan volume in the direct loan program totaled 33 percent at its peak in award year 1997–1998.

Mr. Hinojosa?

Mr. HINOJOSA. Thank you, Mr. Chairman.

General Cuomo, thank you very much for you and your assistant to come and visit with us here in our committee.

My first question is on the basis of your investigation of the relationships between college employees and lenders and the instances you have uncovered of payments or other things of value being exchanged in return to steering borrowers to lenders. Are you considering criminal charges?

Mr. CUOMO. That is a good question, Congressman. These facts present on two levels, if you will. It is the bank-school relationship and then, at times, the bank-financial aid officer relationship. And they are two different concepts.

There is an institutional connection at times between the lender and the school, revenue sharing, printing, et cetera.

And then we have also found cases where they are just—the individual financial aid officer at times unbeknownst to the school has a relationship with a lender and puts that lender as the “preferred lender” and then the phenomenon we discussed before, where the students trust the school, so they go to the preferred lender.

Those are two very different situations for us. And there are a number of cases that my office is investigating where the individual financial aid officer may have been violating laws beyond just the consumer protection laws, and those are ongoing investigations in the office.

And yes, there is a potential for criminal charges in those cases.

Mr. HINOJOSA. My next question is do you think that students and families would be better served if lenders and—if the lenders marketed directly to them?

What is your obligation—what is our congressional obligation to assist students and families, many of whom have limited experience with credit, navigate higher education finance and student loans?

Mr. CUOMO. I think, Congressman, first, the Department of Education should do its job. It should be doing the oversight on the FFEL program and the direct program. I believe the safeguards should be extended to the private loan program.

And then I would urge action on the situation that has been uncovered on the preferred lenders and the revenue sharing and those relationships, and what I believe are distortions made to students and to parents in selecting the loans when they arrive at the school.

And I believe this committee and the Department of Education can resolve that also. And as I said to Congressman Andrews, I believe the industry is crying out for your guidance and your intervention.

There is a crisis. Consumers are worried. And the schools and the lenders are ready to change their ways. They are. You have seen that just from my actions as one state A.G. They want to restore the confidence.

Just give them the guidance and the direction and say, “Here is the new protocol, here is the new behavior, here is the new regulation,” and restore the confidence and we can then answer this question on every campus across the nation.

Mr. HINOJOSA. What do you think if we were to require that students and their parents be given counseling through financial literacy education programs that are available now, so that the student and the parent would make an intelligent decision?

Mr. CUOMO. Congressman, I think the counseling is a good idea. I think that should be combined with—you know, as an affirmative counseling effort, but combine that with stopping the distortive material that they are getting, stopping the bad information and the bad guidance, and prime among that is the “preferred lender relationship,” where they are following the school’s advice, and the school may not be giving that advice in their best interest.

Mr. HINOJOSA. I believe that seeing what has happened in the home mortgage financing industry, where we have had tens of thousands of foreclosures, that we are considering requiring counseling before a mortgage loan is given, and there seems to be a lot of support in Congress for this.

And so I am trying to see how we could also do the same thing for this type of a student loan because, in many cases, particularly in areas that I represent, were it not for a student loan, our students would not be able to access higher education.

And I strongly believe that that is going to be a recommendation that I will be discussing with my colleagues.

I yield back, Mr. Chairman.

Chairman MILLER. I thank the gentleman.

Mr. CUOMO. Congressman, if I might—Mr. Chairman, just in response, I agree with the congressman’s statements wholeheartedly.

And what the housing market did—and I had the opportunity to work with you on some of those issues, Congressman, years back—we provided counseling, but we also fought predatory lending.

To me, this is a fashion of predatory lending. It is not used normally in the college loan context, that term, but it could be, because the same types of tactics we saw that we referred to as predatory lending in mortgages—we are seeing the same tactics in the college loan, and they predatory, and there is predatory lending.

So let’s attack the predatory lending, and let’s put the counseling in place to offer the affirmative guidance.

Mr. HINOJOSA. I thank you.

Chairman MILLER. Congressman Kuhl?

Mr. KUHL. Yes.

Welcome back to Washington, Attorney General.

Mr. CUOMO. Good to see you.

Mr. KUHL. Nice to see a fellow New Yorker here.

Mr. CUOMO. Yes, sir.

Mr. KUHL. Nice to see you also leading the way in what is obviously a very deceptive practice going on today, and I certainly value your testimony.

A couple of things I want to follow up on with what Congressman Hinojosa brought forward. And that is in your testimony, you talk about illegal practices.

I guess it comes from my training as a lawyer as to knowing exactly what you term to be illegal. I have heard general references to violations of consumer protection laws and that sort of thing.

I particularly was interested in the criminal aspects of this particular practice. And before we get there, we are—or I should say—

and you are concentrating primarily on private loans, is that correct?

Mr. CUOMO. That is correct, sir.

Mr. KUHLMAN. Okay. And we recognize, I think, jointly that the Department of Education has no control over private loans at this point, is that correct?

Mr. CUOMO. At this point, that is correct, sir.

Mr. KUHLMAN. Okay. And you are advocating that they do involve themselves in what really is a free market practice right now between a school and—a student, I should say, and a creditor, a bank.

Mr. CUOMO. Well, what I have said about the Department of Education first is they do regulate the FFEL program, as you know.

Mr. KUHLMAN. Right.

Mr. CUOMO. We pointed out a number of instances where the FFEL program—there were violations in the regulations concerning the FFEL program—many of the state schools in our home state of New York, where there are just violations within the FFEL program—current regulations, no additional jurisdiction.

The suggestion is there should also be additional supervision on the private program which would require congressional action, is my guess.

Mr. KUHLMAN. Right. And I think you used the statistic 90 percent of the loans that are given are in that private arena, and that is where you found the violations primarily in your investigation?

Mr. CUOMO. No, Congressman. Ninety percent is the percentage of students that take loans from preferred lenders, the lenders that are on the college preferred list. Ninety percent of the students follow the school's recommendation.

The private loans are, give or take, about 20 percent of the entire loan portfolio nationwide, but it is the percentage of the market that is actually growing dramatically.

Mr. KUHLMAN. Okay. And to follow up on your testimony relative to illegal practices, what illegal—under the statutes of New York that you are sworn to uphold, really occurred in those instances that your investigation revealed?

Mr. CUOMO. There are two different situations, as we discussed. First, under the business laws of the state of New York and the consumer protection laws, it is illegal to have deceptive business practices.

In our opinion, some of these business practices are deceptive, where you are getting a “kickback,” which is the term that we have been using this morning, for a loan that was undisclosed.

You have deceptive business practices, and we protect the New York consumer. So the rationale for the jurisdiction in schools in other states—because if New Yorkers are there, and they are consumers, then we protect the consumers.

Mr. KUHLMAN. Let me just interrupt for just a minute. On that specific point, has there been any kind of proactive attempts to be deceptive by any of the colleges that you have seen, from material that they have advanced?



Or is it an omission act on their part not to disclose their relationship that we are really kind of keying into, or that your investigation keyed into here?

Mr. CUOMO. Both.

Mr. KUHL. Both.

Mr. CUOMO. Both. First, non-disclosure is a problem, Congressman.

Mr. KUHL. I am not debating that it is or isn't. I am just curious from a factual standpoint what your investigation found. If there were schools that were saying—

Mr. CUOMO. Well, almost all of this that we have been talking about this morning is a case of non-disclosure.

Mr. KUHL. Okay. By omission?

Mr. CUOMO. Well, non-disclosure by omission.

Mr. KUHL. Okay.

Mr. CUOMO. You had an economic incentive in the transaction, and you never disclosed your economic self-interest to me.

As a matter of fact, you represented the opposite. You said, "This is good for you, Andrew. We think this is a good business transaction for you, Andrew." And you never told me that you were getting a commission on the business transaction. I consider that deceptive.

On the situations with the individual, that is a different situation, because those are—they are not institutional.

These are individuals who were involved in securities transactions with private companies that violated in some cases the college code, and possibly violated criminal laws.

Mr. KUHL. Okay.

Chairman MILLER. The gentleman's time has expired.

Mr. KUHL. My time has expired. Thank you.

Chairman MILLER. Ms. McCarthy?

Mrs. MCCARTHY. Thank you, Mr. Chairman, and thank you for holding this hearing.

And again, it is good to see you, Attorney General Cuomo. We have worked together in the past, and hopefully we will work together in the future.

I have a little bit of a curiosity. I also sit on Financial Services, and with the banks that you have had statements with, were they breaking any regulations as far as through the banking industries? We have three different regulators of banks.

Are those regulators looking into any of these practices that you have uncovered?

And I guess the biggest thing is you just came into office in January. How long do you think these particular practices have been going on? And how did you pick it up and be able to do something in such a rapid time, when no one else seemed to know what was going on?

Mr. CUOMO. Well, Congresswoman, thank you for the question. And it is a pleasure to be with you once again, and it is a pleasure to be able to work together on yet another important issue to New Yorkers and to Americans.

As far as other banking regulators looking at these issues, I am not aware of that. I wouldn't be surprised, however, because this

is basically a consumer lending transaction where the bank is offering a consumer loan, a student loan.

The schools are almost de facto brokers, in my opinion, when they enter into these relationships where they are receiving a commission.

It is almost like they went into the brokerage business, undisclosed brokers, and they are receiving a commission for their brokerage service.

But I am not the banking regulator. It wasn't my jurisdiction, and we were doing this under consumer protection laws.

In terms of where did this come from, it is interesting. It is an industry-wide practice, Congresswoman, that I believe has evolved over a period of years.

And it is one of those industry practices where it starts small. It becomes more egregious as time goes on. More people are doing it. And then you get to a point where basically everyone is doing it.

Every school seems like they are doing it. Everyone is going to the conferences. Everyone has a preferred list. Everyone has revenue sharing. It must be okay if everyone is doing it.

We have seen these type of situations on Wall Street, where you have a practice that just grows and grows and grows, and it becomes very widespread, and people take comfort in the fact that everyone is doing it, but you scratch the surface and you really look at the underlying rationale, and it collapses.

And I think that is what happened here. I don't believe the oversight was adequate. I don't believe the guidance was adequate. And it grew and it grew and it grew, and people took comfort that everyone was doing it.

And now the expression we use in the office—it is like peeling an onion. One situation leads to another, leads to another, leads to another. And that is what we have been doing over the past several months.

Again, the good news is the industry gets it. I really believe that. The schools get it. The lenders get it. Students understand this issue. And students are now asking the tough questions.

And the industry really does want to reform the practice, because they need to. It is like the housing arena. Consumer confidence drives the market. And they need to restore consumer confidence.

Otherwise, students are unwilling to take the loans, or they are asking a lot of tough questions when they take the loans, and that is actually an opportunity for government.

You are not going to have to fight the market here. You can do it with the market, because the market needs to restore the consumer confidence as much as the consumers need the confidence restored.

Mrs. MCCARTHY. I personally don't buy it that, you know, just because everybody was doing it that no one, whether in the lenders, the bankers or even the schools, had a thought that this could be wrong. I don't understand that.

Obviously, you know, the banks, the lenders—they all have spreadsheets. Money is given. Transactions are done. It is like being on the take. I mean, I am lost on how they didn't think some-

thing was wrong, or not even to report it somewhere, that someone didn't do it.

Is that what we are seeing? Is that what we are facing, that corporations today are saying, "You know, oh, it must be okay?" I mean, I am tired of those excuses, to be very honest with you.

Mr. CUOMO. Well, Congresswoman, I am with you. But that was where this started. Now, it has unfolded rapidly, but a couple of months ago when we started this, that is where it started—everyone does it, there is nothing wrong with it.

Mrs. MCCARTHY. Thank you.

Chairman MILLER. The gentlewoman's time has expired.

Mr. Hoekstra?

Mr. Ehlers?

Mr. EHLERS. Thank you, Mr. Chairman. I apologize for being late, but I had two other committee meetings I had to attend.

Since I have not spent much time here, I am unprepared to ask questions, and I plan to yield time to Mr. Keller.

But I just want to thank you for being here. Thank you for what you have uncovered. I am amazed that we didn't uncover it ourselves earlier. And I hope we can examine all the student loan programs and look at some of the programs.

With that, I am pleased to yield the balance of my time to Mr. Keller.

Mr. KELLER. Well, thank you, Mr. Ehlers, for yielding.

Mr. Attorney General, you said your investigation is like peeling an onion. I can assure you that your investigation, like an onion, has brought tears to many lenders' eyes here.

You have recovered a substantial amount of money, \$6.5 million before today, and then you announced, presumably, a lot more today.

Who controls that money that you have recovered for this national education fund?

Mr. CUOMO. The financial payments happen in two areas. Number one, there are funds that are returned to students primarily from the schools. If we believe there was a payment that was questionable, those payments are turned over to the students.

That is the \$500 per student, University of Pennsylvania, and that has been the majority of the arrangements with the schools.

Mr. KELLER. Let me just stop you on that. First, if it goes to the school with directions, do you use it for need-based financial aid, or for anything they want, or how does that work?

Mr. CUOMO. No, the schools will return—I use the expression return the money to the students, because my position is that the students subsidized that payment to the school.

So the school will return the money to the students who took loans that year and proportionate to their loan amount. So if you took a larger loan than I took, you get more money back than—

Mr. KELLER. And that is most of the—say most of the \$6.5 million you recovered so far will go back to the schools, at those particular schools?

Mr. CUOMO. Well, that is one aspect of funding. Another aspect of funding is primarily from the lenders, where it is not a question of returning money to students.

My office is going to run an educational program to educate high school students and parents about the loan programs, the benefit of programs, but it will be obviously an objective source of information for high school students and their parents.

Congressman Hinojosa's point, I think, was very well taken. The counseling aspect of this is also important.

Understanding the FFEL versus direct versus Stafford versus Perkins versus private versus PLUS—it gets confusing, especially for a high school student who hasn't had a lot of experience in this area, so we will offer an educational program in that regard.

Mr. KELLER. All right. And your office will decide with respect to those funds from the lenders where that money will be spent?

Mr. CUOMO. Yes, sir.

Mr. KELLER. And so it is a national education fund, so will it be distributed equally among the states like Florida, or is New York going to be on the preferred list of receiving those funds?

Mr. CUOMO. Well, we have a lot of New York students in Florida schools. We have a lot of New Yorkers who move to Florida. So it is going to be a prime market for us.

Mr. KELLER. We will look closely at that list and make sure it is not preferred there.

Let me ask you something about this preferred list issue, anyway. Clear it up for me. It would seem to some of us that maybe you want to do away with preferred list altogether, but then on the other hand you have wholeheartedly endorsed Congressman Miller's Sunshine Act, which doesn't do away with the preferred list. It just says you have to have a minimum of three.

Where do you stand on this issue about whether we should do away with the preferred list or keep them?

Mr. CUOMO. You can either fix it, reform it, or do away with it. You can't leave it the way it is. I don't believe that is an option.

If you want to regulate it and reform it, you can keep it. If you don't believe you have the capacity to do the oversight or the appetite to do the reform, then do away with it.

I am not against preferred lender lists per se, because—just the way I am running an educational program to inform high school students, because this is complicated.

If you have a college that says, "I will undertake voluntarily the task of vetting all these lenders, and I will bring them in, and I will do the interviews, and I will go through the loan rates, and I will go through the service records, and I am going to recommend three or four or five lenders to my student population, only on their best interest," the school says, "I have no conflict of interest. My financial aid officer has nothing to do with the universities. This is just a gratuitous opinion to help my students," that could be a good thing.

But then it has to be regulated. First of all, there have to be regulations. Then those regulations have to be enforced. Then there has to be oversight. And you could do that. And that is a position I endorse.

Or do away with the list. If we don't believe we have that capacity, then say the schools should not be making recommendations, should not be steering, because they may be self-interested, and that could actually be hurting the consumer interest of the student.

Mr. KELLER. Thank you. My time has expired.

Chairman MILLER. Thank you.

Mr. Bishop?

Mr. BISHOP OF NEW YORK. Thank you, Mr. Chairman. Thank you very much for holding this hearing.

Mr. Attorney General, welcome, and we New Yorkers have been proud to call you one of our own for a long, long time, but we are particularly proud right now. So thank you very much for the work that you have done.

Mr. CUOMO. Thank you.

Mr. BISHOP OF NEW YORK. Let me start with an observation. It is not remotely surprising, in my view, that the private loans have grown so dramatically in recent years. And in part, they have grown because of federal policy or federal actions.

You know, college costs are increasing. Only very recently did we increase the Pell grant maximum for individual students. We have kept campus-based federal funding constant, I think, since 2000 or 2001.

The president's budget request to Congress suggested that we eliminate SEOG, eliminate Perkins loans. So we are leaving needy students with precious few options if they are going to attend the colleges of their choice.

What I want to focus on—you have testified and you have said that you think the lenders get it. You think the schools get it. You think that they want to reform themselves. You have entered into 16 or 17 agreements with schools and agreements with four lenders.

Does your office have the staff to monitor compliance with these agreements on an ongoing basis, or is that monitoring of compliance better left to the federal government?

Mr. CUOMO. Congressman, first, thank you very much for your kind words. We can monitor the agreements that we have signed. We can monitor the 16 schools. We can monitor the four lenders. Our agreements were done in such a way that they are relatively simple to monitor.

Can we replicate the task that the Department of Education should be doing? Of course not. Could even all the attorneys general combined be replicating the task of the Department of Education? I don't believe so.

And that is why there is a federal government. There are state attorney generals.

But I think the best course is, as a believer in the federal government, as a former Cabinet secretary who truly has the highest respect for federal service, I believe through this committee and the Department of Education federal policy should be set.

Regulations should be promulgated now for effect. This is not a question where we need task forces and study groups before we act. Pass the regulations. Do the oversight.

Mr. BISHOP OF NEW YORK. On the issue of preferred lender list, I know we have talked about this throughout the morning, but our legislation basically deals with the issue of preferred lender list in terms of greater transparency and having schools provide clear information as to how and why a school came—pardon me, a lender came to be on a preferred lender list.

Do you believe that is sufficient, or do you think we should have more extensive monitoring, if you will, or more extensive efforts to control how preferred lender lists are developed?

Mr. CUOMO. Congressman, I think you answered both ends of the equation—the how and why did you pick the lender, and it can only be with the interest of the students in mind. And number two, there are no conflicts for the school or the financial aid officer.

If those two conditions exist, then I think the preferred lender list can be an asset.

Mr. BISHOP OF NEW YORK. Thank you. And thank you very much for—

Mr. CUOMO. Thank you. Pleasure being with you.

Chairman MILLER. Congresswoman Shea-Porter?

Ms. SHEA-PORTER. Thank you, Mr. Chairman.

And thank you very much for being here and for your testimony. I am very concerned about, first of all, the culture that we have been discussing. It feels like a corrupt culture, and I have to agree with the congresswoman who said it feels like on the take.

And I don't understand it. And I am concerned, and I wanted to read a couple of things that I had seen in an A.P. article, when they are talking about a senior department student aid official placed on leave pending an investigation of \$100,000 in stock in Education Lending Group, the former parent company of Student Loan Express.

Do we have a problem inside the Department of Education here?

Mr. CUOMO. I don't know if we have a problem inside the department, Congresswoman, just because I haven't done that work, and it is not my role.

But I agree with the congresswoman and Congresswoman McCarthy and Congressman Hinojosa on the point that there are instances of just plain, blunt corruption here.

We have found those instances primarily around the financial aid officer situations, where individuals in the financial aid office basically undertook self-dealing, I believe in violation of the law.

So there are instances of corruption, there is no doubt.

Ms. SHEA-PORTER. Okay. Also, in the A.P. article it talked about lenders also would not be allowed to pay college employees to serve on advisory boards.

That would seem like a no-brainer right away, that you wouldn't have a college employee on an advisory board of a lender. Is that very common?

Mr. CUOMO. We have found it. But, Congresswoman, your basic point I agree with, which is we have to change the culture here. It is not just a question of a specific fact pattern. There is a culture.

There are relationships here which have to be changed and broken, and relationships between the financial aid officers and lenders, relationships between the schools and lenders. And there has to be a new code of conduct, we call it, a new culture defining those relationships.

Ms. SHEA-PORTER. Perhaps an old code, because I think back when I was in college, and I don't think we needed all these laws. People understood, instead of us having to constantly address it.

And I wanted to disagree with something a colleague across the aisle said when he was talking about the Department of Education and wondering if, you know, it should have a role.

It is not the Department of Education. It is the political people inside the Department of Education that appear to be falling down on this job.

And so my next question to you is why can't we just have the federal government—when we look at the problems that we are having with these preferred providers and others, are they absolutely a necessary component?

I know when I got my student loans we just had a couple of choices. Life was easy. Paying back wasn't, but, you know, we understood what the responsibility was. And we didn't have to maneuver through all of this.

I look at my own daughter who is in college, and every single day—and she is not even living at home—I receive for her an application for a credit card company and for this and for that.

Is there a way—is there some harm in simplifying this and saying, "If you go to college, you are going to get your loan, these are the federal loans that are available, and we are not going to put out a menu with 10,000 different companies?" Is there something inherently wrong with that?

Mr. CUOMO. Congresswoman, it is a good question. I don't know the area well enough, frankly, to say whether or not there could be a consolidation of these different programs.

I ran the Department of Housing and Urban Development as secretary for 4 years and then assistant secretary for 4 years, and the constant question was, "Why do we have to have so many housing programs? Can't we consolidate these? It is so confusing."

There is old language at HUD and housing and different programs and different acronyms. I don't know student lending well enough to say whether or not there could be a consolidation of programs.

And also, competition is a good thing. I believe that. And putting lenders in competition, who can get the rates down for students, and who can offer the best package—that is a good thing.

That is just not what we have now. We have almost the opposite. We have a virtual monopoly for lenders where 90 percent of the students are going to a selected group of lenders. The monopoly, if you will, is done through the preferred lender list.

And the preferred lender list can be a very good thing and can help guide the students through the maze that you are discussing. But then it has to be done on the student's interest, and there can't be conflicts.

Ms. SHEA-PORTER. Okay, thank you. My time has expired. Thank you.

Chairman MILLER. Thank you.

Mr. McKeon just wanted to make a clarification. Then Mr. Courtney is next.

Mr. McKEON. Thank you, Mr. Chairman.

Just in clarification, most of the dealings that you had with these different schools really involved private lending, is that correct?

Mr. CUOMO. Private lending and FFEL programs.

Mr. McKEON. But most of it—the majority was private lending.

Mr. CUOMO. We have had activity in both. I would have to look at how many cases we have done in each to answer your question.

Mr. McKEON. What we have seen so far that you reported—most of it was private lending, which we have no—and the department has no jurisdiction over. It comes under another committee, the Financial Services.

And also, in the refunding or—what do we call that?—the revenue sharing—that is already against the law with regard to the FFEL program. We have already done that. So it is the private lending, which we have no jurisdiction over now.

If we could go to Mr. Franks and ask him to give up that jurisdiction, that would be great, and we could get it all here where we could get our hands on it.

Chairman MILLER. He doesn't even have to give it up. He would just agree with us. We are talking to the committee. Obviously, there is a number of issues here that stray off in different directions and different jurisdiction.

Once again, we would like jurisdiction not to become the issue here. We would like the results of Mr. Cuomo's investigation and our own legislation and others to be the results of that, not a jurisdictional fight.

Mr. CUOMO. But just to clarify—

Chairman MILLER. Mr. Courtney?

Mr. CUOMO. Excuse me, I am sorry. Just to clarify on the congressman's point, the Marist College case that we discussed—that is the FFEL program. New York Institute of Technology—that is the FFEL program.

Columbia University—that is the FFEL program. SUNY, state university system of New York, had a college that was engaged in a FFEL program violation.

So we are talking about FFEL program violations as well as, as the congressman points out, private loans.

Mr. McKEON. And those are the areas that our bills that we have introduced we would have—

Mr. CUOMO. Yes.

Mr. McKEON [continuing]. We would have a chance to address.

Chairman MILLER. We will come back. Mr. Courtney can see his time evaporating.

Mr. Courtney is recognized for 5 minutes.

Mr. COURTNEY. Thank you, Mr. Chairman.

And I want to congratulate the attorney general on the fine work you are doing. Mr. Blumenthal, your neighbor next door, I know is working hard to get Connecticut covered as well.

Mr. CUOMO. Oh, he is the dean. He is a great, great man.

Mr. COURTNEY. I will tell him you said so. When Congresswoman Shea-Porter talked about how it is hard to almost understand how much change has gone on for families dealing with this issue, I mean, one reason I think the change is happening is that going to college now is like buying a house in terms of the size of the cost.

And that really has just raised the stakes for everybody in terms of what—as consumers, but certainly in terms of lenders as well, in terms of what type of money people can make out of this process.



And you know, using the house analogy, I mean, it strikes me that the preferred lender list is almost like saying to people buying a home, "You know, we are going to let the home builder select the top two or three banks that you can buy your house through."

And there almost seems to be something almost inherently—a conflict with having the entity that you are paying be involved at all in the decision-making.

And it seems to me that using another sort of example where the government had to come in and sort of straighten out a marketplace that was out of control was the situation with Medicare supplemental insurance about 10 years or so ago, where, again, consumers were being overwhelmed and confused with insurance companies that were selling Medicare supplemental insurance policies and ending up with products that weren't what they were purported to be.

And the government had to step in and basically structure the marketplace with the A through J different types of plans, and then allow the insurance companies to compete on price, which has worked actually pretty well in terms of making sure that at least from a consumer protection standpoint insurance policies did cover a basic set of coverages.

But it still allowed a marketplace to give people a choice in terms of price. And I know you have tried to sort of balance your testimony in terms of not castigating the notion of preferred providers list as a—you know, as an option as we move forward.

But it just seems to me that at some point, you know, it is a situation in which given, again, the amount of money that people are having to use in terms of student loans that maybe colleges and universities really should just be sort of taken out of this process and allow the government to set up a separate mechanism for protecting the consumer.

Mr. CUOMO. Well, Congressman, let me respond, and let me be more direct. Sometimes as a New Yorker I am a little too reserved and indirect, I have found.

Mr. COURTNEY. We haven't noticed that at Fenway Park.

Mr. CUOMO. And Congressman Bishop made this point earlier. This is a double whammy for students and the reason I have a disagreement with the point that Congressman McKeon raised.

What is really happening is this. The cost of a college education has skyrocketed. The student loans don't give the student enough money to pay for the education. The student's only alternative is to go to the private loans "alternative."

The joke is because they have no alternative. That is why they are taking a private loan, at an exorbitant interest rate, because federal programs don't provide enough money to pay the tuition, period.

So if you want to go to college, you take the federal loans, then you have to take a private loan. Otherwise you can't afford it.

When you go to the private loans, they are a function of the private marketplace. There are no caps. There is a high potential for abuse. They are very expensive.

When you compare this market, this industry, to the housing mortgage market, in my opinion there is no comparison. The housing mortgage market is much safer than this market.

These issues of disclosure, these conflicts of interest are much better protected in the mortgage arena than they are in the student loan arena.

The “predatory lending” that we have talked about in the housing market arena is a modified version of what we are looking at in the student lending arena.

So I agree that many students take the private loans as a last resort because they can’t afford the school. They are unregulated. There is a high potential for abuse. The abuse has happened.

It is not as well regulated as the housing market, not that that is perfectly regulated either, and not that there is not abuse there, but there are many more regulations than you have in the lending area.

And it is a situation that is only getting worse. And I would like to see a more aggressive federal response than we have seen thus far.

Mr. COURTNEY. Thank you, Mr. Chairman.

Chairman MILLER. Mr. Hare?

Mr. HARE. Thank you, Mr. Chairman. Thank you for holding the hearing this morning.

And, Attorney General Cuomo, thank you very much for coming and for all the hard work you have done.

And I am happy that on Monday the attorney general of my state, Lisa Madigan, worked with you, and because of those efforts two for-profit college systems with headquarters in Illinois, DeVry University and Career Education Corporation, agreed to make changes in their student loan practices and to adopt the code of conduct that you have been talking about for lenders and colleges alike.

You know, I don’t know how many times today I have heard the term kickback, but it would seem to me—and I agree with Mr. Payne.

You know, for those students, you know, the \$500 per person, I wonder if for those people who were basically allowed to be used, if you will—and hopefully the \$500 will help them—if you went into a convenience store in my state, I believe it is—and you lifted \$500 worth of merchandise, I think that would be a felony.

And it just seems to me that this kind of conduct is just absolutely insane. And it is wrong. And I just want to, you know, commend you for the work you have done.

I just want to ask you, on the basis of your investigations and the relationship between these employees and the lenders, are you considering filing criminal charges against any of the folks that have been found to have practiced and engaged in this?

Mr. CUOMO. There is a possibility of criminal charges against the—in some of the cases that we are investigating, yes, Congressman.

And I also agree with you. The expression I used is the private loans are the Wild West of student lending. And I believe the federal government does have a responsibility.

And we know there are abuses. We know that it is the area that is growing. We know that it is highly unregulated now.

And we know that you are dealing—you are preying on a population of students who are not in the position to protect themselves and don't really have any alternatives or options.

And why shouldn't the federal government give them the protection? And I believe this committee can do it, or the committee could do it working in conjunction with another committee if there is a jurisdictional debate.

But I think what the consumers across the country are saying is, "Please help." And I am sure this committee intends to respond.

Mr. HARE. One other question I wanted to ask you was about the chairman's bill that I am a co-sponsor of, and I know you support the Student Loan Sunshine Act.

And from your perspective, if you could tell me or maybe the committee why you feel that the act is so important and, you know, why we need it.

I mean, I think I know that, but I am just wondering from your perspective.

Mr. CUOMO. Well, I think, Congressman, on a number of levels. Number one, students need help. Parents need help.

Number two, the industry itself needs confidence restored. And again, we have four of the top lenders in the country—the four top lenders in the country—just in the past month entered into settlements with us.

Sixteen schools all across the country, just in the past month—this is an industry that is crying out for reform and crying out for a new standard. There is no one better, nobody better, at providing a national uniform reform standard than the federal government.

And change comes in a number of ways. And we have done change through the states, through attorneys general, when the federal government has failed to act. We did it on Wall Street when the SEC failed, in my opinion. We have done it in the environment when EPA has failed.

Arguably, we are doing it now where the Department of Education has failed. But it is not the best way to do it. I believe the best way to do it is with deliberate federal action, not federal inaction where the states fill the void.

Mr. HARE. Attorney General, if you wouldn't mind, I would like to—with the remainder of my time, Congresswoman Shea-Porter, I think, has a very important question. I think I will let her ask it.

But again, I just want to thank you for all your hard work and continued success in this field. Thank you very much.

Mr. CUOMO. Thank you. It is a pleasure to work with Lisa Madigan. She is a real pro.

Ms. SHEA-PORTER. Thank you very much, Congressman.

I wanted to ask a question about a federal database and if these lenders have had any access to it. I read that recently they have been banned from accessing a federal database. Was there any abuse there?

Mr. CUOMO. I only know what I have read in the papers on that issue, Congresswoman. I don't have any independent knowledge. But I think the stopping of the access to the database was a good idea.

Ms. SHEA-PORTER. Okay. Thank you.

And I yield back. Thank you.

Chairman MILLER. Thank you.

Attorney General, you have been very generous with your time, and I told you I would get you out of here at a reasonable time. I think I am a few minutes beyond what we agreed to, but thank you.

Mr. CUOMO. Still reasonable, Mr. Chairman.

Chairman MILLER. It is unusual to have one witness have to field all of the questions. Usually you get to share them with a panel.

But this has been, I think, very helpful to us, hopefully helpful to the public in terms of understanding what has taken place here and what you have uncovered along with the other attorney generals.

I appreciate your remarks and your support of my legislation, Mr. McKeon's legislation, and we are going to try to respond to this in a timely fashion.

But again, thank you so much for your leadership and your actions that you have taken to date on this matter, and it is great to have you here in this capacity as the attorney general of the state of New York.

Thank you very, very much.

Mr. CUOMO. It is good to be back, Mr. Chairman. Thank you.

Chairman MILLER. The committee record will remain open for members for the next 14 days if members have submissions that they want to make.

I think some members may have additional questions, Mr. Attorney General, that they may want to submit to you in writing. If that is all right with you, we would like to be able to do that.

Mr. CUOMO. It is my pleasure.

Chairman MILLER. And with that, the committee will stand adjourned.

[The prepared statement of Mr. Altmire follows:]

**Prepared Statement of Hon. Jason Altmire, a Representative in Congress  
From the State of Pennsylvania**

Mr. Chairman, thank you for holding this important hearing on unethical practices that have been discovered in the student loan industry.

I would also like to thank Attorney General Cuomo for taking the time to be here today. I appreciate your leadership on this issue and look forward to hearing your testimony.

Ensuring that higher education is affordable and accessible to all students is an issue of great importance to me. The state of Pennsylvania has the fifth most expensive public institutions of higher education and the tenth most expensive private institutions of higher education. As a result, loans are an essential part of financing education for most students in Pennsylvania and getting the best possible interest rates is crucial to making higher education affordable and accessible to them.

This Congress has already taken a great first step in making college more affordable for students by passing the College Student Relief Act (H.R. 5), which reduces the interest rate on subsidized student loans from 6.8% to 3.4% over the next five years. Eliminating the unethical practices that have been found in the student loan industry, and therefore, helping students and their families receive the best possible deal is the necessary next step.

I am aware that most lenders and institutions of higher education are not bad actors, and that many lenders have begun dealing with the issues that have come to light. Today, I am interested in learning how Congress can best help make sure that all lenders and institutions of higher education are held to the same high ethical standards.

Thank you again, Mr. Chairman, for holding this hearing. I yield back the balance of my time.

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[Additional submission from Mr. Platts follows:]

**Additional Submission From Mr. Platts**

Thank you, Chairman Miller. In response to a request from the Pennsylvania Higher Education Assistance Agency (PHEAA), which has an office in my Congressional District, I am submitting for the record the Education Lending Code of Ethics which PHEAA and the American Education Services (AES) recently adopted.

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[Statement of the PHEAA and AES follows:]

**Prepared Statement of the Pennsylvania Higher Education Assistance Agency (PHEAA) and American Education Services (AES)**

*Education Lending Code of Ethics*

As America's leading non-profit student aid organization, the management of the Pennsylvania Higher Education Assistance Agency (PHEAA) and American Education Services (AES) have adopted the following Education Lending Code of Ethics as part of an effort to help ensure integrity in all aspects of the federal student loan program.

This Code of Ethics formalizes long-standing business practices. This Code of Ethics reflects PHEAA & AES' unique role as a federal student loan guarantor, servicer and lender, and as Pennsylvania's legislatively-created agency responsible for administering the Pennsylvania State Grant and other state-funded programs. This Code of Ethics supports PHEAA & AES' mission to provide affordable access to higher education.

*No Revenue Sharing Between PHEAA and the School*

PHEAA & AES will continue its practice of not providing postsecondary schools with any financial benefits in exchange for a competitive advantage or preferential treatment. PHEAA & AES will continue the policy of not providing monetary incentives to secure a position as a school's recommended lender.

*Gift and Trip Prohibitions*

In its role as a student loan lender, PHEAA & AES will not provide postsecondary school employees with anything exceeding a nominal value. This includes a strict prohibition on trips for financial aid administrators and other college officials paid for by PHEAA & AES.

*Student Loan Advisory Boards*

In its role as a student loan lender, PHEAA & AES will not provide postsecondary school employees with anything of value in exchange for their service on an advisory board or compensate them for their service on an advisory board. PHEAA & AES value the views of the financial aid community and will continue to seek their input on programs and services.

*Preferred Lender Guidelines*

PHEAA & AES believe that the practice of schools recommending lenders for federal and private loans should be based on the cost of the loan, the ease and speed of application and funds disbursement and superior customer service; all of which focus on the best interests and needs of students with no direct regard for any financial benefit to the school.

*Preferred Lender List Disclosure*

PHEAA & AES support transparency in the way lenders are recommended including the criteria used in recommending lenders. Students and families must be informed that they may select the lender of their choice. In all such events, and to safeguard against predatory lenders, the school should provide information to the student on the best possible loan options, with the most favorable terms, customer service, and lender integrity.

*Student Loan Resale Disclosure & Borrower Protections*

PHEAA & AES pledge to honor all borrower benefits that are promised to and earned by borrowers, regardless of which lender originated the student loan. PHEAA & AES believe that all lenders should make the same pledge to help safe-

guard the borrower's long-term financial interests. Lenders should also disclose to borrowers at the time a loan is originated if they intend to sell their loans to another entity.

*Customer Service Integrity*

PHEAA & AES' customer service representatives have not and will not identify themselves to students, families or borrowers as employees of any school. Nor will PHEAA & AES employees physically work in or provide staffing to a school's financial aid office. Furthermore, PHEAA & AES pledge to continue to locate its industry-leading customer service call centers in the United States, using highly trained employees to best serve the individual needs of students and their families.

*About PHEAA, Powered by AES*

PHEAA is the nation's leading nonprofit student aid organization. We devote our energy, resources and imagination to developing innovative ways to ease the financial burden of higher education for students, families and taxpayers.

Our public service mission is powered by American Education Services (AES), our commercial business enterprise. The earnings generated by AES through loan guaranty, loan servicing and student aid processing systems fund our \$72.5 million supplement to the State Grant Program, millions of dollars in free scholarships and loan forgiveness, award-winning online planning tools and the nation's lowest-cost student loans—all at no cost to taxpayers.

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[Whereupon, at 12:16 p.m., the committee was adjourned.]

